

BEFORE THE
TENNESSEE STATE BOARD OF EQUALIZATION

In Re: EchoStar Satellite, LLC)
 Personal Property Account Nos. P-164095, P-164325,)
 P-164326, P-164327, P-164328, P-164329, P-170613) Shelby County
 Tax year 2004)

INITIAL DECISION AND ORDER

Statement of the Case

The Shelby County Board of Equalization ("county board") has valued the subject property for tax purposes as follows:

<u>Account No.</u>	<u>Appraisal</u>	<u>Assessment</u>
164095 (Memphis)	\$250,900	\$75,270
164325 (Arlington)	\$ 21,800	\$ 6,540
164326 (Collierville)	\$ 34,800	\$10,440
164327 (Unincorporated)	\$ 7,600	\$ 2,280
164328 (Germantown)	\$ 23,900	\$ 7,170
164329 (Millington)	\$ 39,500	\$11,850
170613 (Bartlett)	\$ 10,000	\$ 3,000

On November 26, 2004, the taxpayer filed appeals with the State Board of Equalization ("State Board").

The undersigned administrative judge conducted a hearing of this matter on August 23, 2006 in Memphis. The appellant, EchoStar Satellite L.L.C. ("Echostar"), was represented by Senior Property Tax Manager John Spillner. Assistant Shelby County Attorney Thomas Williams appeared on behalf of the Shelby County Assessor of Property ("Assessor"). Also in attendance at the hearing were the Assessor's Audit Manager, Eric Beaupre, CPA, and Director of Finance, Gwendolyn Cranshaw, CPA.

Findings of Fact and Conclusions of Law

Background. EchoStar, a Colorado-based limited liability company, is a satellite television service provider doing business as “DISH Network.” In tax year 2004, EchoStar timely filed personal property reporting schedules for all of the subject accounts with the Assessor’s office pursuant to Tenn. Code Ann. section 67-5-903. However, in his cover letter of February 25, 2004, Property Tax Manager Patrick Sullivan asserted that the satellite receivers and related equipment listed on those returns were non-assessable “inventories of merchandise held for sale or exchange” as defined in Tenn. Code Ann. sections 67-5-901(b) and section 67-

4-702(a)(9).¹ Mr. Sullivan cited as supporting authority the opinion of the undersigned administrative judge in Memphis CATV (Time Warner Entertainment Co., LP) (Shelby County, Tax Years 1999-2000, Initial Decision and Order, December 13, 2002). Alas, the subject property was assessed on the basis of standard depreciated cost; and the county board upheld the Assessor's values.

On March 15, 2005, the State Board issued an interlocutory order in the Memphis CATV case affirming the administrative judge's conclusion that unreported cable television converter boxes and remote controls were leased property not assessable to the company.² The Board reasoned in pertinent part as follows:

Time Warner's customers were free to rent cable control equipment from Time Warner or others while still obtaining cable service from Time Warner. In this sense the equipment has become a consumer product not unlike a television the customer may buy or rent from various sellers.

But in a cautionary footnote, the State Board added that:

...[T]his conclusion is not required in all circumstances. For example, equipment which a taxpayer must necessarily obtain from Time Warner in order to utilize particular Time Warner services, may be considered for assessment purposes to be so subsumed within the service that the existence of a true lease is refuted. Such equipment, not apparently at issue here, may still perhaps be considered business equipment of a service provider for assessment purposes rather than a consumer product available for lease or purchase. [Emphasis added.]

These appeals by EchoStar, which had been held in abeyance pending resolution of the key Memphis CATV issue, were heard several days after entry of the Assessment Appeals Commission's final order in that case (subject to State Board and/or judicial review).

EchoStar purportedly leases (or holds for lease) the satellite receivers and other components (e.g., remote controls; Smart Cards; dish antennas; and low noise block converters with integrated feeds) covered under the terms of its standard customer agreement. Exhibit B. This "12-month lease" agreement requires payment of what EchoStar calls an *equipment rental fee*; however, this monthly fee – typically \$5.00 per receiver – is commonly included in the package price for the selected programming. Exhibit C. Echostar's financial statement for the year ended December 31, 2003 shows upwards of \$244 million in "equipment leasing" income. Exhibit A.

Upon expiration or termination of the so-called lease, the customer must bear the expense of returning all of the covered equipment (except the satellite dish) to EchoStar, or pay

¹Mr. Sullivan explained in his letter that the company was reporting this property "to avoid any arbitrary forced assessments."

²Tennessee is apparently the only state in the country in which leased personal property in the possession of the lessee is assessed to the lessee. See Tenn. Code Ann. section 67-5-901(b).

a substantial "equipment and installation services charge." This equipment remains "the exclusive property of DISH Network"; and the customer has "no right to purchase" it at any time.

Unlike modern cable television converters, satellite receivers are not "addressable"; that is, they are not two-way communication devices.³ There are two manufacturers of DISH Network systems in the United States. Through an affiliated business entity, EchoStar ships this equipment to various retail outlets such as RadioShack and Sears Roebuck.⁴

The vast majority of Dish Network subscribers "lease" their equipment from EchoStar. But according to Mr. Spillner's testimony, such equipment may also be purchased from retail stores as well as "secondary tier vendors" over the Internet.⁵ See Exhibit E. Ironically, to the best of his knowledge, consumers could no longer obtain the kind of cable television equipment that was deemed not to be assessable in Memphis CATV from any source other than the cable company.⁶

Yet, in his research prior to the hearing, Mr. Beaupre found no place of business in Shelby County which actually stocked a new DISH Network receiver for sale. He did not consider the agreement signed by EchoStar's customers to be a "true lease" of personal property.

Contentions of the Parties. Though it has never filed a business tax return with the Shelby County Clerk, EchoStar contends that the property in question is not assessable under Tenn. Code Ann. sections 67-5-901 *et seq.* because the company is *subject to* the Business Tax Act.

In his post-hearing memorandum, Mr. Williams denies that EchoStar has substantiated its claim of exemption of the subject property from ad valorem taxation.

Applicable Law. Article II, section 28 of the Tennessee Constitution provides (in relevant part) that "all property real, personal or mixed shall be subject to taxation" unless exempted by the legislature; and that:

The Legislature shall have power to tax merchants, peddlers, and privileges, in such manner as they may from time to time

³It is the connection of a satellite receiver with a land-based telephone line that enables the customer to order programming directly and the company to track usage.

⁴These retailers are not parties to the service agreement between the customer and EchoStar; rather, they are merely agents of the company with respect to the activation of service.

⁵At the hearing, the administrative judge requested Mr. Spillner to submit as a late-filed exhibit a copy of the contract form which was supposedly executed by those DISH Network subscribers who own their own equipment. It turned out, as acknowledged in Mr. Spillner's letter of September 6, 2006, that EchoStar "does not require customers, who own their satellite TV receiving equipment, to sign a customer agreement. They simply pay month to month based on the programming package they purchased."

⁶Mr. Spillner attributed this fact to the technological development of the cable TV industry.

direct, and the Legislature may levy a gross receipts tax on merchants and businesses in lieu of ad valorem taxes on the inventories of merchandise held by such merchants and businesses for sale or exchange.

Accordingly, the Business Tax Act expresses “the legislative intent that the taxes imposed by this part shall be in lieu of any or all ad valorem taxes on the inventories of merchandise held for sale or exchange **by persons taxable under this part.**” Tenn. Code Ann. section 67-4-701(b). [Emphasis added.]

As the party seeking to change the current assessments of the subject property, EchoStar has the burden of proof in this administrative proceeding. State Board Rule 0600-1-.11(1)

Analysis. For all practical purposes, at least as of January 1, 2004, EchoStar was the sole supplier of the sophisticated technical equipment necessary for receipt of DISH Network programming. Such equipment is not only manufactured to the company’s specifications by a limited number of vendors, but also marketed exclusively through authorized distributors and participating dealers.

Of course, some consumers may be able to obtain *possession* of a new DISH Network satellite system or component through independent sources. But even aside from the difficulty experienced by Mr. Beaupre in locating such product within Shelby County, nothing in the documentary evidence of record suggests that EchoStar has sanctioned the outright sale of DISH Network equipment to consumers as a regular business practice. Indeed, it seems counterintuitive to suppose that a satellite television company whose customers have no contractual right to purchase its equipment would routinely transfer *ownership* of such merchandise to consumers through retail channels.

Hence the property in question does not appear to be what the State Board characterized in Memphis CATV as “a consumer product...the customer may buy or rent from various sellers.” Nor, in the opinion of the administrative judge, is such personal property truly “leased” in the sense contemplated by Tenn. Code Ann. section 67-5-901(b). By Mr. Spillman’s own admission, this equipment has no utility other than for the procurement of DISH Network programming.⁷ Contrastingly, the utility of the cable converters and remote controls in the Memphis CATV case was “not wholly linked to the service offered by the company.” Initial Decision and Order at p. 8.

Like the contract security company involved in Sonitrol of Memphis, Inc. (Shelby County, Tax Years 1996 through 1998, Initial Decision and Order, August 4, 2000), EchoStar is essentially engaged in the delivery of services – not the sale or lease of products *per se*. In

⁷Thus it is surely understandable that, notwithstanding EchoStar’s recognition of “equipment leasing” income in an accounting sense, the monthly rental fee (based on the number of receivers) would be included in the programming package price.

Sonitrol, the taxpayer argued that the alarm and surveillance systems installed by the company were "leased" to its clients. This theory was rejected on the rationale that:

...[T]he taxpayer has not relinquished such control over the property in question that it may legitimately be considered "leased" for ad valorem tax purposes. From a business standpoint, that is hardly surprising; for Sonitrol undertakes private protective services that are dependent on precise placement, operation, and maintenance of its security equipment. The taxpayer's capability to perform those services would obviously be impaired if its customers were permitted to use, alter, or move such equipment however they saw fit.

Id. at p. 8.

Similarly, EchoStar may terminate an agreement at any time if the customer "transfer(s), encumber(s) or relocate(s) the equipment" (Exhibit B); and, according to the "Residential Customer Agreement" posted on EchoStar's Web site (Exhibit 2), "[a]ll maintenance and repair of the equipment shall be performed by us or our designees." This contractual language leaves EchoStar largely in control of what amounts to business equipment.

For these reasons, the instant case is distinguishable from Memphis CATV, and does not warrant the same result.

Order

It is, therefore, ORDERED that the subject property be assessed as determined by the county board.

Pursuant to the Uniform Administrative Procedures Act, Tenn. Code Ann. §§ 4-5-301—325, Tenn. Code Ann. § 67-5-1501, and the Rules of Contested Case Procedure of the State Board of Equalization, the parties are advised of the following remedies:

1. A party may appeal this decision and order to the Assessment Appeals Commission pursuant to Tenn. Code Ann. § 67-5-1501 and Rule 0600-1-.12 of the Contested Case Procedures of the State Board of Equalization. Tennessee Code Annotated § 67-5-1501(c) provides that an appeal **"must be filed within thirty (30) days from the date the initial decision is sent."** Rule 0600-1-.12 of the Contested Case Procedures of the State Board of Equalization provides that the appeal be filed with the Executive Secretary of the State Board and that the appeal **"identify the allegedly erroneous finding(s) of fact and/or conclusion(s) of law in the initial order";** or
2. A party may petition for reconsideration of this decision and order pursuant to Tenn. Code Ann. § 4-5-317 within fifteen (15) days of the entry of the order. The petition for reconsideration must state the specific grounds upon which relief is requested. The filing of a petition for reconsideration is not a prerequisite for seeking administrative or judicial review.

This order does not become final until an official certificate is issued by the Assessment Appeals Commission. Official certificates are normally issued seventy-five (75) days after the entry of the initial decision and order if no party has appealed.

ENTERED this 22nd day of September, 2006.



PETE LOESCH
ADMINISTRATIVE JUDGE
TENNESSEE DEPARTMENT OF STATE
ADMINISTRATIVE PROCEDURES DIVISION

cc: John Spillner, Sr. Property Tax Manager, EchoStar Satellite, LLC
Thomas Williams, Assistant Shelby County Attorney
Eric Beaupre, Shelby County Property Assessor's Audit Manager
Tameaka Stanton-Riley, Mgr. Appeals Department, Shelby County Assessor's Office

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